



1131 SW Klickitat Way
Seattle Washington
98134
800/422-3505 tel
206/623-0179 fax
www.carrix.com

CARRIX, INC.

**STATEMENT FOR THE RECORD
BEFORE THE SELECT REVENUE MEASURES SUBCOMMITTEE
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES**

HEARING REGARDING THE WAYS AND MEANS "DISCUSSION DRAFT"

November 29, 2011

Mr. Chairman, Ranking Member Neal, and distinguished Members of the Committee,

On October 26, 2011, Ways and Means Committee Chairman Camp (R-MI) released a discussion draft of proposed legislation that would significantly amend U.S. international tax rules in the direction of a territorial, or dividend exemption, system (the "Proposal") for comment. In addition, the Proposal reduces the maximum corporate tax rate from 35% to 25%.

Carrix, Inc. ("Carrix") is pleased to submit written comments for the record in connection with the Proposal.

Background on Carrix:

Carrix is a **closely held** U.S.-based port terminal operating company that manages more cargo terminals than any other company in the world. Carrix provides a full spectrum of transportation services, from terminal management to stevedoring, in a number of U.S. and foreign ports.

As a company built on international trade, Carrix fully appreciates the goal of the Proposal: lowering the corporate tax rate and reforming our international tax laws to a territorial regime. The Proposal should make U.S. companies more competitive vis-à-vis their foreign competitors. Carrix, like many other U.S.-based companies in all sectors of the economy, faces fierce competitive pressure from foreign-based companies. Unlike most other U.S.-based companies, many of our foreign-based competitors are large foreign multinationals, some of which are closely aligned with foreign governments, and operate under more favorable home country tax regimes.

Provision of Concern:

In general, Section 301 of the Proposal provides a 95% dividends-received deduction for foreign-source dividends from CFCs (and companies electing to be treated as CFCs), subject to a 365 day holding period. Carrix believes Section 301 of the Proposal imposes tax at a much higher rate than intended on a small group of closely held US multinational companies that are subject to the Personal Holding Company ("PHC") rules established under Sections 541 through 547 of the Internal Revenue Code.

Background on the Personal Holding Company rules:

The PHC tax was enacted in 1934 and, at the time, represented an appropriate response to prevent individuals from sheltering investment income from individual income tax by using their closely held US corporations to hold investments. At the time the maximum individual income tax rate was substantially higher than the maximum corporate tax rate and corporations could be liquidated on a tax-free basis. Neither possibility exists today because of changes to the tax laws, yet the PHC provisions were never updated to reflect more modern circumstances, particularly closely held consolidated groups with foreign affiliates.

The PHC rules impose a corporate level penalty tax of 15% (the rate will become 39.6% in 2013 if the Bush tax cuts expire as scheduled at the end of 2012) on the undistributed PHC Income of a PHC. A corporation constitutes a PHC if 60% of its adjusted gross income is PHC income and if 50% of its stock is owned by five or fewer individual shareholders at any time during the last half of the taxable year. PHC income generally is defined as interest, dividends, royalties, rents, and certain other types of passive investment income. The PHC penalty tax can be avoided by an entity by distributing PHC income to its shareholder(s), resulting in the shareholder(s) paying the appropriate tax on the distribution.

In the case of a group of US corporations filing a consolidated return, the PHC calculations are generally conducted on a consolidated basis. However, in certain circumstances the PHC test and tax computation must be made on a separate company basis. Section 542(b)(2) provides the PHC test must be applied on a separate entity basis if more than 10 percent of an entity's adjusted ordinary gross income is received from a source outside the affiliated group (such as foreign subsidiaries) and more than 80 percent of such adjusted ordinary gross income is PHC income. PHC income would include dividends from foreign subsidiaries.

For each taxable year, if any separate entity included in the affiliated group fails the test under Section 542(b)(2), the entire corporate structure is tainted and each separate entity is potentially subject to the PHC tax. Thus, when the test is conducted on a separate company basis, a US group of corporations filing a consolidated return can easily find that it has a personal holding company tax liability even though a majority of its consolidated revenue may be active trade or business income and it would not otherwise be subject to the PHC tax except for the rules requiring separate company testing.

PHC Rules Applied to the Section 301 of the Proposal:

Under Section 301 of the Proposal, dividends received from eligible CFCs or entities electing to be treated as CFCs would qualify for a 95% DRD.

For companies not subject to the PHC rules (such as public corporations), dividends received from eligible foreign subsidiaries that qualify for the 95% DRD, end up with an effective tax rate of 1.25%. Thus if an eligible dividend received a \$100M dividend from an eligible foreign entity, it would be subject to only \$1.25M of tax (\$5M taxable dividend x 25% tax rate).

In comparison, companies subject to the PHC rules could potentially be subject to a significantly higher tax rate, especially in the common scenario where the foreign dividends are received by holding company whose only significant income are such dividends, even if a majority of the consolidated groups income is not considered PHC income. Companies in this situation would likely be subject to the PHC tax due to the separate company testing required under Section 542(b)(2).

As mentioned above, the 15% PHC penalty tax applies to undistributed PHC income. In calculating the undistributed PHC income, DRDs must be added back; therefore the PHC tax could apply to 100% of the dividend rather than just the 5% per Section 301 of the Proposal.

For example, if a subsidiary in a consolidated group subject to the PHC rules on a separate company basis received a \$100M dividend from an eligible foreign subsidiary, and the entire dividend was subject to the PHC tax, the group member could be subject to \$16.06M of tax, calculated as follows

Income Tax	
Dividend	100,000,000
DRD	(95,000,000)
Taxable Income	5,000,000
Income Tax Rate	25%
Income Tax	1,250,000
PHC Tax	
Taxable Income	5,000,000
Add back of DRD	95,000,000
Less Accrued Taxes	(1,250,000)
Undistributed PHC Income	98,750,000
PHC Tax Rate	15%
PHC Tax	14,812,500
Total Tax for PHC Company on \$100M Dividend	
Income Tax	1,250,000
PHC Tax	14,812,500
Total Tax	16,062,500

Thus the tax would be a 1285% increase in tax (16.06/1.25) compared to companies receiving the same dividend that are not subject to the PHC tax. If the Bush tax cuts expire, the total tax for the separate company subject to the PHC tax in this example would increase to \$40.4M.

Proposed Solution:

A proposed solution would eliminate the provisions that require certain consolidated groups of corporations to determine their PHC tax liabilities on a separate company basis.

This solution would not eliminate the PHC tax for a consolidated group of corporations that is determined to be a PHC on a consolidated basis. However, provided that a consolidated group of corporations is determined not to be a PHC on a consolidated basis, these corporations would not pay the additional 15% penalty tax, but would simply pay the same level of corporate tax as a similarly situated publically traded corporation.

Suggested Legislative Text:

- (a) In General. – Section 542(b) is amended by –
 - (1) striking paragraph (2) and (4), and
 - (2) redesignating paragraphs (3), and (5) as paragraphs (2) and (3) respectively.
- (b) Conforming amendments –
 - (1) Section 542(b)(1) is amended by striking “paragraphs (2) and (3) and inserting “paragraph (2)”.
 - (2) Section 1504(c)(2)(B)(ii) is amended by striking “section 542(b)(5)” and inserting “section 542(b)(3).
- (c) Effective Date – The amendment made by this section shall apply to taxable years beginning after December 31, 2012.

Conclusion:

Thank you for the opportunity to submit these written comments for the record. Carrix looks forward to working with you and your staff to ensure that the U.S. tax code is reformed in a way that makes sense, treats similarly situated taxpayers equally, and doesn't penalize certain taxpayers due to certain antiquated provisions of the Internal Revenue Code.